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CLERK

IN THE

# Supreme Court of the United States

OCTOBER TERM, A. D. 1945

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No. 966

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HERBERT L. STERN,

*Petitioner,*

vs.

CARTER H. HARRISON, Collector of Internal  
Revenue,

*Respondent.*

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## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

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Herbert L. Stern, by A. J. Pflaum, Harry N. Wyatt, Richard H. Levin and Hedwig F. Brann, his counsel, prays that a writ of certiorari be issued to review the judgment of the United States Circuit Court of Appeals for the Seventh Circuit in this case.

**STATEMENT OF MATTER INVOLVED.**

During 1935 and 1936 Balaban & Katz Corporation (hereinafter for convenience sometimes referred to as "B & K"), a corporation engaged in the operation of motion picture theatres in Chicago, adopted a plan for refinancing or recapitalization, designed to substitute low interest

bank loans for high yield securities (notes and preferred stock), thereby diminishing its annual charges before common dividends. During 1936, as one step in the carrying out of this plan, B & K acquired by redemption approximately 50% of its outstanding preferred stock. The petitioner, who was a preferred stockholder of B & K at that time, realized a gain of \$22,650.16 upon this disposition of his stock and treated this gain in his 1936 income tax return as a capital gain subject to the percentage limitations of Section 117(a) of the Revenue Act of 1936. (This statutory provision and the other pertinent statutory provisions here involved are quoted in full in the Appendix hereto.)

This treatment was contested by the Commissioner of Internal Revenue on the theory that the payment by B & K for preferred stock in 1936 was governed by Section 115(c) of the Revenue Act of 1936 as "amounts distributed in partial liquidation of a corporation" and hence the gain on such payment was 100% taxable. The petitioner paid the deficiency claimed and proceeded in the regular form to seek a refund of the amount so paid.

The District Court held that the sale of the preferred stock was one step in and could not be dissociated from the plan of refinancing or recapitalization, that there was no distribution in partial liquidation of B & K within the meaning of Section 115(c) and that the gain was subject to the percentage limitations of Section 117(a).

On appeal by the respondent, the Circuit Court of Appeals for the Seventh Circuit held that the findings of the District Court were subject to review, that the transaction was a distribution in partial liquidation of the corporation within the meaning of Section 115(c) and that the gain was 100% taxable.

## JURISDICTION.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925, c. 229, § 1, 43 Stat. 938; 28 U.S.C.A. § 347(a). The judgment herein sought to be reviewed is a decision of the United States Circuit Court of Appeals for the Seventh Circuit entered December 18, 1945 (R. 132).

## QUESTIONS PRESENTED.

1. Was the finding of the District Court, that the sale of preferred stock here involved was one step in and could not be dissociated from the plan of refinancing and re-capitalization of B & K and hence that payment for said stock was not a distribution in partial liquidation, subject to review by the Circuit Court of Appeals?
2. Were the amounts received by the petitioner on the sale of his B & K preferred stock in 1936 "amounts distributed in partial liquidation of a corporation" within Section 115(c) of the Revenue Act of 1936?

## REASONS FOR ALLOWANCE OF WRIT.

1. In reviewing and reversing the findings of the District Court herein, the Circuit Court of Appeals has assumed authority which it would not have had, under the applicable decisions of this Court, if the decision of first instance herein had been entered by the Tax Court of the United States.

*Dobson v. Commissioner*, 320 U. S. 489;

*John Kelley Company v. Commissioner*, .... U. S.  
...., 90 L. ed. 257.

The question whether the rule of reviewability shall be different for decisions of the Tax Court and decisions of the District Courts involving the same issues is an important question of Federal law which has not been but should be settled by this Court.

2. The decision of the Circuit Court of Appeals that the findings of the District Court herein are reviewable is in conflict with the decision of the Circuit Court of Appeals for the Fifth Circuit to the effect that the rule of *Dobson v. Commissioner*, 320 U. S. 489, is applicable on review of decisions of the District Court.

*Blumenthal Print Works v. United States*, 141 F. (2d) 211 (CCA 5th).

3. The decision of the Circuit Court of Appeals that the redemption of stock in the present case was "automatically" a "distribution in partial liquidation of a corporation" as provided in Section 115(c), without reference to the attendant circumstances and without reference to the form, history and intention of the applicable statutory provisions, is in conflict with applicable decisions of this Court to the effect that definitions in the revenue laws must not be read mechanically so as to force the application of the law to transactions never intended to be covered.

*Gregory v. Helvering*, 293 U. S. 465;

*Pinellas Ice & Cold Storage Company v. Commissioner*, 287 U. S. 462;

*Guy v. Donald*, 203 U. S. 399, 406;

*Helvering v. Morgan's, Inc.*, 293 U. S. 121, 126.

4. Said decision of the Circuit Court of Appeals is in conflict with decisions of other Circuit Courts of Appeals in the same matter, to the effect that a redemption or cancellation of stock may not be dissociated from all of the attendant facts and circumstances so as to characterize the

transaction as a distribution in liquidation of a corporation where the transactions taken as a whole are not in substance liquidating.

*Commissioner v. Whitaker*, 101 F. (2d) 640 (CCA 1st);

*Commissioner v. Kolb*, 100 F. (2d) 920 (CCA 9th);  
*Helvering v. Schoellkopf*, 100 F. (2d) 415 (CCA 2d);

*Helvering v. Leary*, 93 F. (2d) 826 (CCA 4th);  
*Gutbro Holding Company v. Commissioner*, 138 F. (2d) 16 (CCA 2d).

These reasons are further and more fully developed in the brief in support hereof, annexed hereto.

All of which is respectfully submitted.

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